

Battling Unemployment
A First Draft Report Presented to the
Minister of Labour and Social Policy
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I. Recommendations

Get the Real Picture

No one in Macedonia knows the real picture. How many are employed and not reported or registered? How many are registered as unemployed but really have a job? How many are part time workers – as opposed to full time workers? How many are officially employed (de jure) – but de facto unemployed or severely underemployed? How many are on “indefinite” vacations, on leave without pay, etc.?

The Statistics Bureau must be instructed to make the gathering and analysis of data regarding the unemployed (through household surveys and census, if necessary) – a TOP PRIORITY.

A limited amnesty should be declared by the state on violations of worker registration by employers. All employers should be given 30 days to register all their unregistered and unreported workers – without any penalty, retroactive or prospective (amnesty). Afterwards, labour inspectors should embark on sampling raids. Employers caught violating the labour laws should be heavily penalized. In severe cases, closures should be enforced against the workplace.

The Minister of Justice, in collaboration with the court system, should accord the persecution of violating employers a high and urgent priority.

The number of trade inspectors should at least be tripled, as per standards in other developing countries.

All the unemployed must register with the Employment Bureau once a month, whether they are receiving benefits, or not. Non-compliance will automatically trigger the loss of the status of “unemployed”. If a person did not register without good cause, he would have the right to re-register, but his “unemployment tenure” will re-commence from month 1 with the new registration.

I recommend instituting a **households’ survey in addition to a claimant count.** Labour force surveys should be conducted at regular intervals –

regarding the structure of the workforce, its geographical distribution, the pay structure, employment time probabilities.

The statistics Bureau should propose and the government should adopt a Standard National Job Classification.

The Unemployment Benefits

Unemployment benefits – if excessive and wrongly applied – are self-perpetuating because they provide a strong disincentive to work.

Health insurance should be separated from unemployment benefits. Unemployment benefits and health benefits should be paid independently of each other.

Unemployment benefits should be means tested. There is no reason to pay unemployment benefits to the children of a multi-millionaire. Unemployed with assets (especially liquid assets) should not receive benefits, even if they are otherwise eligible. The benefits should scale down in accordance with wealth and income.

Unemployment benefits should always be limited in time, should decrease gradually and should be withheld from certain segments of the population, such as school dropouts, those who never held a job, (in some countries) women after childrearing.

Eligibility to unemployment benefits should be confined to those released from work immediately prior to the receipt of the benefits, who are available to work by registering in an employment bureau, who are actively seeking employment and who pass a means test. Benefits should be withheld from people who resigned voluntarily or discharged due to misconduct or criminal behaviour. In the USA, unemployment compensation is not available to farm workers, domestic servants, the briefly employed, government workers and the self-employed.

Unemployment benefits should not exceed short-term sickness benefits (as is the case in Canada, Denmark and the Netherlands). Optimally, they should be lower (as is the case in Greece, Germany and Hungary). Alternatively, even if sickness benefits are earnings-related, **unemployment benefits can be flat** (as is the case in Bulgaria and Italy). In Australia and

New Zealand, both sickness benefits and unemployment benefits are means tested. It is recommended to reduce the replacement rate of unemployment benefits to 40% of net average monthly wages in the first 6 months of benefits and to 30% of net average monthly wages thereafter in the next 6 months.

Unemployment benefits should be limited in time. In Bulgaria, they are limited to 13 weeks, in Israel, Hungary, Italy and the Netherlands to 6 months and in France, Germany, Luxemburg and the United Kingdom – 12 months. Only in Belgium are unemployment benefits not limited in their duration. In most of these, countries, though, social welfare payments replace unemployment benefits following the prescribed period of time – but they are usually lower than the unemployment benefits and serve as a disincentive to remain unemployed rather than employed. It is recommended to limit the duration of unemployment benefits to 12 months.

No health insurance should be paid for those unemployed for more than 6 months.

No unemployment benefits should be paid to a person who refuses work offered to him or her on any grounds, except on medical grounds.

I recommend a few pilot projects with the aim of implementing them nationwide, should they prove successful:

A pilot project should be attempted to provide **lump sum block grants** to municipalities and to allow them to determine eligibility, to run their own employment-enhancement programs and to establish job training and child care assistance. An assessment of the success or failure of this approach in a limited number of municipalities can be done after one year of operation.

The unemployed worker, who participates in the second pilot project, should be provided with a choice. **He could either receive a lump sum or be eligible for a longer period of unemployment benefits.** Alternatively, he can be provided with a choice to either receive a larger lump sum or to receive regular unemployment benefits. In other words: he will be allowed to convert all or part of his unemployment benefits to a lump sum. The lump sum should represent no more than 9 months of unemployment benefits reduced to their net present value (NPV).

The **state should provide matching funds** if the person chooses to establish a business, alone or in partnership with other unemployed people (provide credits of 1 euro or a state guarantee for 1 euro against every 1 euro invested by the unemployed person).

The third pilot project involves the formation of **private unemployment insurance plans** to supplement or even replace the insurance (compensation, benefits) offered by the Employment Fund. In many countries, private unemployment insurance is lumped together with disability and life insurance – all offered by the private sector within one insurance policy.

The fourth and last pilot project involves the formation of **“Voucher Communities”**. These are communities of unemployed workers organized in each municipality. The unemployed exchange goods and services among themselves. They use a form of “internal money” – a voucher bearing a money value. Thus, an unemployed electrician can offer his services to an unemployed teacher who, in return will give the electrician’s children private lessons. They will pay each other with voucher money. The unemployed will be allowed to use voucher money to pay for certain public goods and services (such as health and education). Voucher money will not be redeemed or converted to real money – so it has no inflationary or fiscal effects, though it does increase the purchasing power of the unemployed.

Encouraging Employers to Hire the Unemployed

The principle governing any incentive scheme intended to encourage employers to hire hitherto unemployed workers must be that the employer will get increasing participation in the wage costs of the newly hired formerly unemployed workers – more with every year the person remains employed. Thus, a graduated incentive scale has to be part of any law and incentive plan. Example: employers will get increasing participation in wage costs – more with every 6 months the person has been unemployed by them.

Additionally, employers must undertake to employ the worker a number of months equal to the number of months they received benefits for the worker and with the same salary. It would be even better if the incentives to the employer were to be paid for every SECOND month of employment. Thus, the employer would have an incentive to continue to employ the new worker.

Employers will receive benefits for a new worker only if he was registered with an unemployment office for 6 consecutive months preceding his new employment.

I recommend linking the size of investment incentives (including tax holidays) to the potential increase in employment deriving from the investment project.

ALTERNATIVE TEXT PROPOSED BY MACEDONIAN EXPERTS

There are two types of incentive schemes intended to encourage employers to hire hitherto unemployed workers.

In the first method the employer gets increasing participation in the wage costs of the newly hired formerly unemployed workers – more with every year the person remains employed. Thus, a graduated incentive scale has to be part of any law and incentive plan. Example: employers will get increasing participation in wage costs – more with every 6 months the person has been unemployed by them.

In the second method (preferrable in Macedonia's conditions), employers must undertake to employ the worker a number of months equal to the number of months they received benefits for the worker and with the same salary. It would be even better if the incentives to the employer were to be paid for every SECOND month of employment. Thus, the employer would have an incentive to continue to employ the new worker.

Employers will receive benefits for a new worker only if he was registered with an unemployment office for more than 12 consecutive months preceding his new employment – or if he or she is a recipient of welfare payments and social benefits through the Employment Bureau. This is much like the very successful American and British schemes of “Welfare to Work”.

I recommend linking the size of investment incentives (including tax holidays) to the potential increase in employment deriving from the investment project.

Encouraging Labour Mobility

Workers must be encouraged to respond promptly and positively to employment signals, even if it means relocating. We recommend **obliging a worker to accept any job offered to him in a geographical radius of 100 km from his place of residence.** Rejection of such work offered (“it is too far”) should result in a loss of the “unemployed” status and any benefits attaching thereof. On the other hand, the **Employment Bureau should offer financial and logistical assistance in relocation and incentives to relocate to areas of high labour demand.** The needs of the unemployed worker’s family should also be considered and catered to (kindergarten or school for his children, work for his wife and so on).

Fixed term labour contracts with a lower cost of dismissal and a simplified procedure for firing workers must be allowed (see details below).

I recommend **altering the Labour Relations Law to allow more flexible hiring and firing procedures.** Currently, to dismiss a worker, the employee has to show that it has restricted hiring, applied workforce attrition and reduced overall overtime prior to dismissing the worker. The latter has recourse to the courts against the former. This recourse should be eliminated and replaced with conciliation, mediation, or arbitration (see below for details).

Reforms in the Minimum Wage

The minimum wage is an obstacle to the formation of new workplaces (see analysis in the next chapter). It needs to be reformed.

I propose a **scaled minimum wage**, age-related and means tested and also connected to skills.

In other words, the minimum wage should vary according to age, other (non-wage) income and skills.

Administrative Measures: Early Retirement

Macedonia must allow the employer to **encourage the early retirement of workers** which otherwise might be rendered technologically redundant.

Early retirement is an efficient mechanism to deal with under-employment and hidden unemployment.

Romania ameliorated its unemployment problem largely through early retirement.

Offering a severance package, which includes a handsome up-front payment combined with benefits from the Employment Fund, can encourage early retirement. A special **Early Retirement Fund** can be created by setting aside receipts from the privatization of state assets and from dividends received by the state from its various shareholdings, to provide excess severance fees in case of early retirement.

ALTERNATIVE TEXT PROPOSED BY MACEDONIAN EXPERTS

An employer with technologically redundant employees should be allowed to offer to them the following retirement scheme:

1. They will be considered pensioners for the purposes of every applicable law and benefit (for instance, for the purposes of the Health Fund).
2. Thus, they will not be “fired” but “retired”.
3. Upon retirement, they will receive a lump sum, which will represent their compensation for their accumulated work tenure, in accordance with the law (=their severance fee).
4. They will begin to receive monthly pension payments, as per their entitlement, work tenure, level of last salary, etc. only when they reach the age prescribed by law (63 – 65) – LIKE EVERY OTHER PENSIONER.

NOT RECOMMENDED Administrative Measures: Reduction of Working Hours

Another classic administrative measure (lately implemented in France) is a **reduction in the standard working week** (in the number of working hours). For reasons analyzed in the next chapter, we recommend NOT to implement such a move, despite its obvious (though false) allure.

NOT RECOMMENDED Administrative Measures: Public Works

All the medically capable unemployed should be compulsorily engaged in **public works** for a salary equal to their unemployment benefits (Workfare). A refusal by the unemployed person to be engaged in public works should result in the revocation of his “unemployed” status and of all the benefits attaching thereto.

Generally, we would not have recommended public works.

From the Encyclopedia Britannica:

“The weakness in the proposal to use disguised unemployment for the construction of social overhead capital projects arises from inadequate consideration of the problem of providing necessary subsistence funds to maintain the workers during the long waiting period before the projects yield consumable output. This can be managed somehow for small-scale local community projects when workers are maintained in situ by their relatives – but not when workers move away. The only way to raise subsistence funds is to encourage voluntary savings and expansion of marketable surplus of food purchased with these savings.”

But public works financed by grants or soft loans can serve as an interim “unemployment sink” – a buffer against wild upswings in unemployment.

The situation in Macedonia is so extreme, that it is comparable only to the Great Depression in the USA.

In the USA, in 1932, the Civilian Conservation Corps (CCC) was established to tackle nature conservation work for the young and unmarried men. They planted trees, erected flood barriers, put out forest fires and constructed forest roads and trails. They lived in work camps under a semi-military regime. They were provided with food rations and a modest monthly cash allowance, medical care and other necessities. The CCC employed 500,000 people at its peak – and 3 million people throughout its existence.

In any case, there is always the danger that public works will simply displace existing employment. Labour union and local municipality endorsements should, therefore, be strictly observed.

Administrative Measures: Public Education and Dissemination of Information – The Functioning of the Employment Bureau

The dissemination of information regarding employment practices, opportunities, market requirements, etc. should be a prime component of the activity of the Employment Bureau. It must transform itself from a mere registry of humans to an **active, computerized exchange of labour**. This can be done through computerized employment exchanges and intermediation.

To **change the image of the Employment Bureaus** from places where the unemployed merely registers and receive benefits to a labour exchange can be done by publishing examples of successful job placements.

I recommend to **prominently display and disseminate information** regarding the rights of the unemployed, their obligations and services available to them and to publish weekly or daily employment bulletins.

I recommend to **place computer terminals in all bureaus** with the latest data regarding jobs offered and sought. Both employers and the unemployed should be able to **directly access and update** the system from PCs or laptops or by submitting forms.

To organize **seminars for the unemployed and to employers** in which the rights of the unemployed, their obligations and the services offered to them and to their potential employers will be described. This can be combined with employment fairs. Separately, the unemployed should be taught in these seminars how to find a job, prepare a curriculum vita (biography), entrepreneurial skills, preparation of business plans, marketing plans, feasibility studies, credit applications and interview skills.

The Employment Bureaus in collaboration with the local authorities should organize **job clubs, labour exchanges and employment fairs** – places where employers can meet potential employees, currently unemployed. These should not be one-off, haphazard events. They should be periodic, regular, and predictable.

I recommend to **oblige the mass media by law to dedicate at least an hour weekly** (could be broken to as many as 4 segments of 15 minutes each) to unemployment: disseminate information, organize a televised labour

exchange, a televised entertainment show (where employers will offer a job to a winner) and so on.

I recommend to link by a **Wide Area Network (WAN) or Intranet with firewalls the National Employment Bureau, the Health Fund, the Pension and Disability Insurance Fund and the Social Security Office.** To cross and compare information from all these bureaus on a real time basis (to specifically cater to the needs of an unemployed person) and on a periodical basis for supervision and control purposes.

The National Employment Bureau should maintain a **regular presence in employment fairs abroad.** Many fairs are global and work can be obtained in them for Macedonian workers (especially the more skilled).

I recommend the creation of a **special office within the Ministry of Labor and social Work with the aim of actively soliciting employment abroad** for qualified and skilled Macedonians (from construction workers to computer programmers). This office will:

- Scan for job offers in foreign countries
- Make contact with government structures, public sector, and private sector employers abroad
- Sign agreements with said employers and negotiate with them all employment terms and conditions. These terms and conditions are bound to be better than anything individual laborers can obtain by themselves.
- Advertise for workers in Macedonia, based on the agreements afore signed.
- Match workers with job offers abroad, based on the signed agreements.
- Self-finance by collecting a commission based on a the first pay of every placed worker.

A National employment Contract

A “National Employment Contract” should be signed between the government, the trade unions, the employers (Chamber of Commerce) and the Central Bank. All parties will have to concede some things.

The Employers will guarantee the formation of new work places against a freeze on employee compensation, a separate treatment of part time labour (exclusion from collective bargaining), flexibility on minimum wages and with regards to job security, hiring and firing procedures, social and

unemployment benefits, indexation of wages and benefits, the right to strike and the level of salaries.

The employers will obligate themselves to fixed quantitative targets over a number of years against the receipt of the unemployment benefits of the newly hired (or another form of subsidy or tax incentive) and/or a discount in social contributions.

The National Employment Contract should aim to constrain inflation by limiting wage gains to productivity gains (for instance, through dividends on the shareholdings of the workers or through stock options schemes to the workers).

In return, the trade unions will be granted effective control of the shop floor. This is the neo-corporatist approach.

It means that the tripartite social contract will increase employment by moderating wage demands but the unions will control policies regarding unemployment insurance, employment protection, early retirement, working hours, old age pensioners, health insurance, housing, taxation, public sector employment, vocational training, regional aid and subsidies to declining and infant industries.

In Sweden and Germany there is co-determination. Workers have a quasi-constitutional shop floor representation even in non-wage related matters (such as the work organization).

Many countries instituted an “Incomes Policy” intended to ensure that employers, pressurized by unions, do not raise wages and prices. In Sweden, for instance, both labour and management organizations are responsible to maintain price stability. The government can intervene in the negotiations and it can always wield the whip of a wage freeze, or wage AND price controls. In Holland the courts can set wages. Wages and unemployment benefits are perceived as complementary economic stabilizers (contra the business cycle).

Another possibility is a Guaranteed Wage Plan – Employers assure minimum annual employment or minimum annual wages or both to those employees who have been with the firm for a minimum of time.

Firms and trade unions must forego the seniority treatment (firing only the newly hired – LIFO, last in first out). The firm should be given a free hand in hiring and firing its employees regardless of tenure.

Labour Disputes Settlement

The future collective agreements should all be subordinated to the National Employment Contract. All these agreements should include a compulsory dispute settlement through mediation and arbitration. All labour contracts must include clear, compulsory and final grievance procedures. Possibilities include conciliation (a third party bring management and labour together to try and solve the problems on their own), mediation (a third party makes nonbonding suggestions to the parties) and arbitration (a third party makes final, binding decisions), or Peer Review Panels – where the management and the employees together rule on grievances.

A strike will be allowed only AFTER the failure of OBLIGATORY arbitration, mediation, or conciliation procedures.

I recommend allowing out of court settlement of disputes arising from the dismissal of employees through arbitration, an employees' council, trustees or an employer-employee board.

Unconventional Modes of Work

Work used to be a simple affair of 7 to 3. It is no longer the case.

In Denmark, the worker can take a special leave. He receives 80% of the maximum unemployment benefits plus no interruption in social security providing he uses the time for job training, a sabbatical or further education, or a parental leave. This can be extended to taking care of old people (old parents or other relatives) or the terminally ill – as is the case in Belgium (though only for up to 2 months). It makes economic sense, because their activities replace social outlays.

In Britain, part time workers receive the same benefits in case of layoffs and wrongful dismissals and in Holland, the pension funds grant pensions to part time workers.

Special treatment should be granted by law and in the collective agreements to night, shift and weekend work (for instance, no payment of social benefits).

All modes of part-time, flextime, from home, seasonal, casual and job sharing work should be encouraged. For example: two people sharing the same job should be allowed to choose to be treated, for tax purposes and for the purposes of unemployment benefits, either as one person or as two persons and so should shift workers. In Bulgaria, a national part time employment program encouraged employers to hire the unemployed on a short term, part time basis (like our Mladinska Zadruga).

The law should be altered to remove the current upper limit of 6 months imposed on temporary employment. Employers and employees should be allowed to contract freely, for any length of time they find appropriate (and providing they register their contract lawfully).

Macroeconomic Policies

The macroeconomic policies of Macedonia are severely constrained by its international obligations to the IMF and the World Bank. Generally, a country can ease interest rates, or provide a fiscal boost to the economy by slashing taxes or by deficit spending.

Counter-cyclical fiscal policies are lagging and as a result they tend to exacerbate the trend. Fiscal boosts tend to coincide with booms and fiscal contraction with recessions.

In view of the budget constraints (more than 97% of the budget is “locked in”), it is not practical to expect any employment boost either from the monetary policy or from the fiscal policies of the state in Macedonia.

What I do recommend is to introduce a “**Full Employment Budget**” (see details in Appendix number I). A full employment budget adjusts the budget deficit or surplus in relation to effects of deviations from full or normal unemployment. Thus, a simple balanced budget could be actually contractionary. A simple deficit may, actually, be a surplus on a full employment basis and a government can be contractionary despite positive borrowing.

Apprenticeship, Training, Retraining and Re-qualification

The law should be amended to allow for apprenticeship and training with training sub-minimum wages. Mandatory training or apprenticeship is a beneficial rigidity because it encourages skill gaining. Germany is an

excellent example of the benefits of a well-developed apprenticeship program.

Most of the unemployed can be retrained, regardless of age and level of education. This surprising result has emerged from many studies.

The massive retraining and re-qualification programs needed to combat unemployment in Macedonia can be undertaken in collaboration with the private sector. The government will train, re-train, or re-qualify the unemployed worker – and the private sector firms will undertake to employ the retrained worker for a minimum period of time following the completion of his or her training or retraining. Actually, the government should be the educational sub-contractor of the business sector, a catalyst of skill acquisition for the under-capitalized private sector. Small business employers should have the priority in this scheme.

There should be separate retraining and re-qualification programs according to the educational levels of the populations of the trainees and to the aims of the programs. Thus, vocational training should be separated from teaching basic literacy and numeracy skills. Additionally, entrepreneurship skills should be developed in small business skill training programs and in programs designed to enhance the management skills of existing entrepreneurs.

All retraining and re-qualification programs should double as advisory services. . The instructors / guides / lecturers should be obliged to provide legal, marketing, financial, sales-related or other consulting. Student who will volunteer to teach basic skills will be eligible to receive university credits and scholarships.

Entrepreneurship and Small Businesses

Small businesses are the engine of growth and job creation in all modern economies. In the long run, the formation of small businesses is Macedonia's only hope. The government should encourage the provision of micro-credits (from microfinance through to commercial banking) and facilities to set up small and home-based businesses by the banking system. In the absence of reaction from or collaboration with the banking system, the state itself should step in to provide these funds and facilities (physical facilities and services – such as **business incubators**).

Thus, the state should encourage small businesses through **microcredits, incubators, tax credits, and preference to small businesses in government procurement.**

1. The government will encourage the provision of **micro-credits and facilities** to set up small and home-based businesses by the banking system and non-banking special purpose financial institutions.
2. The government – through its network of Employment Bureaus and facilities – will provide entrepreneurs with **physical facilities and services – such as business incubators.**
3. The state will encourage small businesses through the provision of **subsidized and state guaranteed micro-credits.**
4. The government will give domestic investors and domestic entrepreneurs and intrapreneurs (=investments within big firms) the **same treatment accorded to foreign investors**: tax credits, tax holidays, deferral of capital gains taxes and so on.
5. Small to medium size businesses will be given **preference in government procurement and in public tenders.**
6. The government will encourage innovation and the formation of intellectual property by **financing the registration of international patents, brand names, copyrights, and trademarks and by organizing innovation fairs and exhibitions** in Macedonia or participating in such fairs and exhibitions abroad in an effort to locate investors, venture capitalists and risk capital funds for Macedonian inventors and innovators.
7. The government will encourage home businesses by **supporting women entrepreneurs.** This will be done by providing them with the conditions to work and exercise their entrepreneurial skills. By establishing day care centres for their children. By providing micro-credits (microfinance). By giving women special tax credits. By allowing or encouraging flextime or part time work or work from home. By recognizing the home as the domicile of business (especially through appropriate tax deductibles). By equalizing the

legal rights and pay of women with men. By protecting them from sexual or gender harassment.

8. The government will **identify priority future leading economic sectors and act to support them**. The education and higher education systems will be re-directed and encouraged to produce the skills needed by these economic sectors. In Macedonia, these sectors include: designer textiles, off season agricultural products, high value added agricultural products (e.g., greenhouse flowers), organic foods, ethnic foods, remote processing of backroom operation using computers and modems, software authoring and many other sectors where Macedonia has comparative advantages.
9. The government will encourage **community-level and municipality-level economic activities and other civic local initiatives**. This will be done by opening municipal “one stop shops” and by providing financial assistance and participation of the state, either through the banking system or through independent contractors.
10. The government will implement a **“One Stop Shop” approach in all relevant economic legislation and regulation**. It will strive to cut bureaucracy by amending all the laws related to business and trade to include a mandatory “one stop shop” provision.
11. The government will **encourage big firms to reward entrepreneurial and innovating workers, to spin off small businesses, to create in-house incubators and to protect their intellectual property**. This will be done by providing a mixture of tax benefits and direct financial assistance.
12. The government will act to **disseminate knowledge and information regarding business, financing, business-related skills and practices, entrepreneurship, management, and quality control techniques** – both through the mass media or directly, through educational schemes and institutions, both public and private.
13. All senior government officials, including ministers, will meet small business owners and entrepreneurs on a regular basis. The government will establish an inter-ministerial **“Committee for Small Business**

and Entrepreneurship”, chaired by the Prime Minister. This will be a steering committee with executive powers.

COMMENT OF MACEDONIAN LABOR EXPERTS

BUT, empirical research has demonstrated that investors are not lured by tax breaks and monetary or fiscal investment incentives. They will take advantage of existing schemes (and ask for more, pitting one country against another). But these will never be the determining factors in their decision-making. They are much more likely to be swayed by the level of **protection of property rights, degree of corruption, transparency, state of the physical infrastructure, education and knowledge of foreign languages** and “**mission critical skills**”, **geographical position** and **proximity to markets** and **culture and mentality**.

Q: Women start one-third of new businesses in the region: now can this contribution to economic growth be further stimulated?

By providing them with the conditions to work and exercise their entrepreneurial skills. By establishing day care centres for their children. By providing microcredits (women have proven to be inordinately reliable borrowers). By giving them tax credits. By allowing or encouraging flexitime or part time work or work from home. By recognizing the home as the domicile of business (especially through the appropriate tax laws). By equalizing their legal rights and their pay. By protecting them from sexual or gender harassment.

II. The Facts

Labour Mobility, Unemployment Benefits and Minimum Wages

We are all under the spell of magic words such as “mobility”, “globalization” and “flextime”. It seems as though we move around more frequently, that we change jobs more often and that our jobs are less secure. The facts, though, are different.

The world is less globalized today than it was at the beginning of the century. Job tenure has not declined (in the first 8 years of every job) and labour mobility did not increase despite foreign competition, technological change and labour market deregulation. The latter led to an enhanced flexibility of firms and of hiring and firing practices (temporary or part time workers) but this is because many workers actually prefer casual work with temporary contracts to a permanent position.

Granted, people have been and are moving from failing firms and declining industries to successful ones and booming sectors. But they are still reluctant to change residence, let alone emigrate. Thus, jobs remain equally stable in deregulated as in regulated labour markets.

Yet, this phobia of losing one’s job (arising from the aforementioned erroneous beliefs) serves to increase both the efficiency and productivity of workers and to moderate their wage claims.

It is safe to assume that collective bargaining led to increased wages and, thus, to less hiring and less flexible labour markets. It is therefore surprising to note that despite the declining share of unionized labour in two thirds of the OECD countries – unemployment remained stubbornly high. But a closer look reveals why. Both France and the Netherlands (where unionized labour declined from 35% of the actually employed to 26%), for instance, extended the coverage of collective agreements to non-unionized labour. It is only where both union membership and coverage by collective agreements were both reduced (USA, UK, New Zealand, Australia) that employment reacted favourably. Thus, at the one extreme we find the USA and Canada where agreements are signed at the firm or even individual plant level. At the other pole we have Scandinavia where a single national agreement prevails. All the rest are hybrid cases. Britain, New Zealand and Sweden decentralized their collective bargaining processes while Norway and Portugal centralized it. The evidence produced by hybrid cases is not conclusive. Decentralized bargaining clearly reduced wage pressures but centralized bargaining also moderated wage demands (union leaders tended

to consider the welfare of the whole workforce. Still, it seems that it is much preferable to choose one extreme or the other rather than opt for hybrid bargaining. The worst results, for instance, were obtained with national bargaining for specific industries. Hybrid Europe saw its unemployment soar from 3 to 11% in the last 25 years. Pure system USA maintained its low rate of 4-5% during the same quarter century. These opposing moves cannot be attributed to monetary or fiscal policies. This is because all economic policies are geared towards increasing employment. Budget cuts, for instance, depress demand and job formation in the short term but, by lowering real interest rates, they encourage investment and job formation in the longer term.

The cycle is:

Employment protection laws make it hard to fire workers and hard for fired workers to find new jobs. The longer one is unemployed, the lesser the chances of employment. Skills rust and the long term unemployed become the unemployable. Gradually, desperation sets in and the unemployed stop looking for a job. Their absence is conspicuous in that they do not restrain the wages paid to the employed. They have become part of the structural unemployment.

Blanchard and Wolfers studied 20 countries between the years 1960-96. They applied 8 market rigidities to their subjects. The average unemployment increased by 7.2% in this period. But in countries with strict employment protection unemployment rose by double the amount in countries with lax labour legislation. The country with the most generous unemployment benefits saw its unemployment rate grow by five times the rate of the stingiest country. And in countries with highly coordinated wage bargaining, unemployment has grown by four times its growth in countries with decentralized bargaining.

It is difficult to isolate these parameters from the general decline in productivity, the increase in real interest rates and technological change and restructuring. Still, the results are fairly unequivocal. Other research (the 1994 OECD one year study, the DiTella-MacCullough study) seems to support these discoveries:

That flexibility is a good thing. It encourages employment, it leads to higher output and to a higher GDP per capita. The reason a transition from a rigid to a flexible labour market does not yield immediate results is that it increases the participation in the labour force. The rate of unemployment is, thus, affected only later, it lags the changes. But flexibility leads to lower rates of unfilled vacancies and to a lower persistence of unemployment over time.

Unemployment in Europe is structural (in Germany it has been estimated to be as high as 8.9%). It is the cumulative result of decades of centralized wage bargaining, strict job protection laws, and over-generous employment benefits. The IMF puts structural unemployment in Europe at 9%. This is while the USA's structural rate is 5-6% and the UK reduced its own from 9% to 6%. The remedies, though well known, are politically not palatable: flexible wages, highly mobile labour, flexible fiscal policy.

Deregulation makes labour markets more flexible because it forces the worker to accept almost any job. Cutting or limiting jobless benefits has largely the same effect. Employers feel more prone to hire people if they can negotiate their wages with them directly and on a case-by-case basis and if they can fire them at will. Hence the debilitating effect of minimum wages and other wage controls as well as of job protection laws.

But all these steps must be implemented together because of their synergy. Research has demonstrated the impotence and inefficacy of half hearted half measures.

Some hesitant steps have been adopted by the governments of Germany and France (which trimmed jobless benefits), by Italy (which stopped linking benefits to inflation), by Belgium, Spain and France, which reduced the minimum wage payable to young people. Spain established two classes of workers with an increased bargaining power granted to those with permanent employment. Yet, some measures yielded quite unexpected and unwanted results. France legislated a reduced working week. Other countries imposed a freeze on hiring with the aim of attrition of the workforce through retirement. Yet, these last two remedies led to an increase in the bargaining power of the remaining workers and to real wage increases.

The only clear causal relationship is between unemployment benefits and the level of employment. The lower the unemployment benefits, the more people seek work and wages decrease. As a result, firms hire more workers. But, firms hire even more when dismissing workers is made easier and cheaper.

Paradoxically, the easier it is to fire workers, the more workers firms are willing to take on and the more secure workers feel knowing that their chances of being hired are better. They look harder for work and find it, reducing the level of unemployment and the costs to the state of jobless benefits. Having to spend less on unemployment benefits, the government can either cut taxes or improve the allocation of its resources. In both cases the economy improves and provides an added incentive to work. This is because, in a vigorous growth economy, the value of an extra worker is higher than the combined costs of his hiring and firing. This is especially

true since the reservoir of the unemployed is comprised of the unskilled, the young and women, whose remuneration is closer to the minimum wage. In the USA the minimum wage is 35% of the average wage (in France, it is 60%, in Britain it is 45% and in the Netherlands it is declining relative to the median salary). It is a fact that when wages are downward flexible – more lowly skilled jobs are created. A 1% rise in the minimum wage reduces the probability of finding a job by 2-2.5%.

There is a debate raging between the proponents of minimum wages (they reduce poverty and increase the equality of wealth distribution) and their opponents (they destroy jobs). The OECD stated clearly that wage regulation couldn't deal with poverty. The reason is that, as opposed to common opinion, few low paid workers live in low-income households and few low-income households have low paid workers. Thus, the benefits of the minimum wage, such as they are, largely bypass the poor.

Again, it is important to realize that unemployment is not a universal phenomenon. It is concentrated among the young and the unskilled. 11% of all people under the age of 25 in the USA are unemployed, almost three times the national average. A shocking 28% of those under the age of 25 are unemployed in France. The OECD says that a 10% rise in the minimum wage reduces teenage employment by 2-4% in both the high and low minimum wage countries.

In view of these facts, many countries (USA, UK, France) introduce “training wages” – actually, minimum wage exemptions for the young. But the minimum wage is still a high percentage of mean youth earnings (53% in the USA and 72% in France) and thus has a prohibitive effect on youth employment.

There is no disputing the facts that minimum wages compress the earnings distribution and reduce wage disparities between ages and sexes but they have no effect on inequality and the reduction of poverty among households. In US households with less than half the median household income only 33% of the adults have a low paid job (The equivalent figure in the Netherlands is 13% and in the UK – 5%). In most poor households no one is employed at all. On the other hand, many low earners have high paid partners. In the USA only 33% of earners of less than two thirds of the median wage live in households whose income is less than 50% of the national median household income. In the UK the figure is 10% and in Ireland – 3%. In each 5-year period only 25% of low paid Americans are in a poor family at some point (the figure is 10% in the UK).

These statistics show that minimum wages hurt poor families with teenagers (by making teenage employment prohibitive) while benefiting mainly the middle class.

Unemployment and Inflation

Another common misperception is that there is some trade off between unemployment and inflation. Both Friedman and Phelps attacked this notion. Unemployment seems to have a “natural” (equilibrium or homeostatic) rate, which is determined by the structure of the labour market. The natural rate of unemployment is consistent with stable inflation (NAIRU – Non Accelerating Inflation Rate of Unemployment).

Making more people employable at the prevailing level of wages can lower NAIRU. This should lead to a big drop in unemployment together with a tiny increase in permanent inflation. Phelps actually sought to lower NAIRU and raise the incomes of the working poor. Stiglitz calculated that the changing demographics of the labour force and the competition in markets for goods and jobs reduced NAIRU by 1.5% in the USA. R. Gordon, D. Staiger and M. Watson support these findings.

It emerges, therefore, that the gap between the estimated NAIRU and the actual rate of unemployment is a good predictor of inflation.

The Rhineland Model the Poldermodel and Other European Ideas

The Anglo-Saxon variety of capitalism is intended to maximize value for shareholders (often at the expense of all others, including the workers).

The Rhineland model is capitalism with a human face. It calls for an economy of consultation among stakeholders (shareholders, management, workers, government, banks, other creditors, suppliers, etc.)

In the Netherlands there is a Social and Economic Council. Its role is advisory and it is semi-corporatist. Another institution, the Labour Foundation is a social partnership between employees and employers.

But the Netherlands succeeded in reducing its unemployment rate from 17% to less than 5% by ignoring both models and inventing the “Poldermodel”, a Third Way. Wim Duisenberg, the Dutch Banker (currently Governor of the European Central Bank), attributed this success to four elements:

Improving state finances

Pruning social security and other benefits and transfers

Flexible labour markets
Stable exchange rate.

The Dutch miracle started in 1982 with the Wassenaar Agreement in which employers' organizations and trade unions agreed on wage moderation and job creation, mainly through decentralization of wage bargaining. The government contributed tax cuts (which served to replace forgone wage increases). This fiscal stimulus prevented a drop in demand as a result of wage moderation. Additionally, restrictions were placed on social security payments and the minimum wage. For instance, increases in wages were no longer matched by corresponding increases in minimum social benefits. Working hours, hiring, firing and collective bargaining were all opened up to labour market forces. The strict regulation of small and medium size businesses (which drove up labour costs) was relaxed. Generous social security and unemployment benefits (a disincentive to find work) were scaled back. The Netherlands did not shy from initiating public works projects, though on a much smaller scale than France, for instance. The latter financed these projects by raising taxes and by increasing its budget deficit. The result could well be a reduction in employment in the long run (the effect of taxation). In the absence of monetary instruments such as devaluation (due to the EMU), the only remedy seems to be labour market flexibility.

Such flexibility must include a substantial adjustment in sickness benefits, vacation periods, maternal leave and unemployment benefits.

The long term (more than 12 months) unemployment in Europe constitutes 40% of the total unemployment. About HALF of the entire workforce under the age of 24 is unemployed in Spain. It is about 28% in France and in Italy. Germany, Austria and Denmark escaped this fate only by instituting compulsory apprenticeship. But the young become the kernel of long-term unemployment. This is because a tug of war, a basic conflict of interests exists between the "haves" and "have-nots". The employed wish to defend their monopoly and they form labour cartels. This is especially true in dirigiste Europe.

While in the USA, 85% of all service jobs created between 1990-5 paid more than the average salary – this was not the case in Europe. Add to this the immobility of labour in Europe and a stable geographical distribution of unemployment emerges, not ameliorated by labour mobility.

The Dutch model sought to battle all these rigidities:

The Dutch reduced social security contributions from 20% (1989) to 7.9% and they halved the income tax rate to 7% (1994).

They allowed part time workers to be paid less than full timers, doing the same job.

They abandoned sectoral central bargaining in favour of national bargaining – but more decentralized.

They cut sickness benefits, unemployment insurance (benefits) and disability insurance payments (by 10% in 1991 alone – from 80% to 70%).

They made it harder to qualify for unemployment (in 1995 no benefits were paid to those who chose to remain unemployed).

The burden of supporting the sick was shifted to the employer / firm. In 1996, the employer was responsible to pay the first year of sickness benefits.

Even the Dutch model is not a success. More than 13% of the population is receiving disability benefits. Only 62% of the economically active population is in the workforce (the rest dropped out of it).

But compare its experience to France, for instance.

The LOI ROBIEN prescribes that companies should be spared social security obligations for 7 years if they agree to put workers on part time work instead of laying them off. Firms abused the law and restructured themselves at the government's expense.

The next initiative was to reduce the working week to 35 hours. This was based on the “Lump of Labour Fallacy” – the idea that there is a fixed quantity of work and that reducing the working week from 39 to 35 hours will create more jobs. In reality, though, labour demand changes only in response to changes in productivity and in the workings of the labour market itself (rigidities). A cut in the working week reduces productivity and destroys jobs rather than foster job formation.

In Spain, a permanent employee fired is entitled to receive up to 45 days' pay multiplied by his or her tenure in years. The result is that firms are afraid to hire or fire workers. The government – faced with more than 22% unemployment – permitted part time contracts with less job protection. Today, 30% of all employed Spaniards work this way. Yet, this led to the creation of a two-tiered workplace where it is easier to fire the part-timer

(even if he is valuable) rather than the permanent (and better earning) worker. Additionally, wages are thus disconnected from productivity.

MACEDONIA

Summary

As privatization progressed (however flawed in concept and in implementation), unemployment rose. It was the result of redundancies, bankruptcies and restructuring of the new private enterprises. By 1998, more than 92,000 workers were involved in direct privatization. There were more than 210,000 workers involved in all enterprises privatized.

The unemployment rate shot up from 23.5% in 1990 to more than 41% (foreign estimates) today (or 34% officially).

While officially the labour-force stands at c. 800,000 people, in reality it comprises only 600,000 (down from 680,000 in 1990). The number of central government employees has remained fairly stable at c. 17,000. About 2,400 are employed in cooperatives, another 22,600 in the pure private sector and c. 92,000 in firms with mixed ownership.

About 4000 are in government subsidized retraining programs at any given moment. Others are retrained within the Labour Redeployment program run by the Agency of Privatization.

Unemployment compensation recipients rose from 5,400 in 1990 to more than 50,000 in 1997.

Mandatory employer payroll tax contribution is 20% (pension) and the employee pays 8% to the Health Fund.

Numerous laws and legal instruments govern employment and unemployment in Macedonia. Among them:

The Law on Labour Relations, the Law on Employment, the Collective Bargaining Agreement, the Law on Pension and Disability Insurance, the Law on Health Protection at Work, the Law on Labour Inspection, the Law on Industrial Action and the July 1997 Law on Employment and Insurance in the case of Unemployment (now largely defunct).

The most important law by far is the Law on Labour Relations. It regulates the terms and manner of entering employment, the rights of employees, job positions, salaries and other compensation. Unfortunately, it is an extremely general and vague law. The collective agreements, the second most

important legal instruments, are as general and, in any case, they pertain mainly if not solely to their signatories.

The collective agreements usually provide for an “employment trial period”. But the law itself equates the rights of the temporarily employed to those of the permanently employed.

The 1997 law allowed the hiring of workers without the assistance or approval of the Employment Bureau. It demanded that the unemployed should actively seek gainful employment to qualify to receive unemployment benefits. It reduced both the amount and the duration of unemployment benefits payable to certain groups of unemployed workers. It introduced payments of pension contributions and health care fund contributions of registered unemployed workers who are not covered elsewhere (for example, by their parents, or their spouse). The law eliminated special one-time payments to the unemployed who could claim a right to a pension equal to 40% of the average monthly net wages. It mandated the monthly registration of recipients of benefits and the bi-annual registration of all other unemployed. Under this law, workers with 15 years of participation in the workforce and contributions to the fund will receive unemployment benefits for 6 months. Those with more than 25 years will receive unemployment benefits indefinitely. Additionally, employers were allowed to use up to 18 months of unpaid payroll taxes to subsidize the wages of previously unemployed workers hired by them. This provision has been eliminated.

Analysis

There are a few statistical methods used to gauge employment-related data. The easiest, most immediate but least reliable way is to count the number of people registered with the Employment Bureau (“claimants”). A claimant count tends to underestimate unemployment by up to 50% (!) because many people are so desperate that they do not bother to register with the unemployment bureau.

The second method which is more demanding, resource consuming and has a time lag – is also more rigorous and a much better gauge of reality. It is the household survey. Britain, for instance, estimates unemployment using BOTH methods.

The Statistical Bureau in Macedonia defines an Employee as someone who is employed at least one hour in the week prior to being sampled, whether in a part time job or in a permanent, full time one. People attending an apprenticeship program or sentenced to correctional labour are excluded (unlike in Germany, Austria or Denmark).

It follows that the unemployed are people seeking employment. Anyone without a job, but previously employed and recorded in an employment office is defined as an “earlier employed person”. Applicants who held no job before are “first time applicants”.

Self-employed workers are all people included in TRUD-15, a quarterly report filed with the Pension and Disability Fund. This report includes only those currently insured and it, too, does not cover vocational students and apprentices. It is, therefore, safe to assume that the number of the self employed in Macedonia is larger than reported.

If the index representing total employment in Macedonia in 1989 was 100.3 – it was 62 in 1997. The figure for women was marginally higher.

Total employment in the economic sector went down by more than 40% between 1989-97.

The strongest declines were in trade and in tourism and catering. But severe drops were registered in mining and industry, agriculture and fisheries, forestry (which was already depressed in 1989). Only water treatment and management and crafts and trades – actually increased. But construction, transport and communications, and, to a lesser extent, housing, utilities, landscaping, financial, technical and business services also declined.

Total employment in the non-economic sector was almost unaffected !!! Even in sectors such as education, science, culture and information and healthcare and social services, the effects were minimal. And in administration and politics there was actually an INCREASE.

The total employed declined from c. 517,000 (1989) to less than 320,000 in 1997.

The total in the economic sectors declined from 430,000 to 270,000.

The total in the non-economic sectors declined from c. 90,000 to 84,000.

The female population reacted more strongly to the trend. Female employment declined from 133,000 in 1995 to less than 122,000 in 1997.

Less than 73,000 women were employed in the economic sector in 1997, compared to more than 84,000 in 1995. In the non-economic sector, the

figures are 49,000 and 49,000 respectively (in other words, employment in the non economic sector remained stable while even as it declined strongly in the economic sector).

To summarize:

In 1997, all employed people numbered c. 319,453 (of whom 121,666 were women).

In the economic sector: 235,206 (72,359)

In companies with social ownership: 185,522 (70,094), of which 121,663 were in the economic sector (30,835 women).

In privately owned firms the figure is – 22,593 (of whom 21,910 in the economic sector). Women accounted for 10,492 (10,252 in the economic sector) of this number.

2,414 workers (629 women) worked in cooperatives (all part of the economic sector).

Firms with mixed ownership employed 91,988 (31,854 women).

Of these employees, 88,799 (30,548) were in the economic sector.

State owned firms, institutions and organs employed 16,936 workers (8,597 women). Of these only 420 were engaged in economic activities (95 women).

The (monthly) demand for workers declined from 6,619 in 1989 to 1,907 in 1996. Concurrently, monthly layoffs doubled from 1,408 to 2,805. First time applicants for unemployment benefits peaked monthly at 3,847 in 1992 and declined to 2,073 in 1996. This is a bad sign – it indicates growing desperation among the long term (more than 12 months) unemployed.

New hiring virtually collapsed from 1,506 monthly in 1989 to 972 in 1997.

Yet, this grim picture has to be balanced by mentioning that many people are unofficially employed and not registered anywhere.

The total number of employment seekers (in parentheses – the number of women) has gone up from 150,400 (78,075) in 1989 to c. 253,000 (115,000) in 1997. But this is misleading because fully 200,000 people have dropped from the workforce and have given up seeking employment.

First time applicants went up from 116,000 to 186,000 in the same period.

In 1989 only 75,000 unskilled workers were jobless. In 1997 the number almost doubled to 133,000.

And while only 5,800 received unemployment compensation in 1989 – their numbers multiplied by 10 (!) and reached over 50,000 in 1997.

Due to improvements in education on the one hand and to growing desperation on the other hand – almost no people younger than 18 years were looking for jobs in 1997 (only 1,700) compared to 1989 (11,900).

To a large extent, the same is true for the 18-25 age groups. 70,400 sought work in 1989 versus 60,100 in 1997.

But the pernicious and lasting effects of unemployment were more than evident in the next age groups. In the age groups 25-40 the number of employment seekers increased from 55,200 to 135,000 in the same period. The number of people between the ages 40-50 seeking work quadrupled (!) from 10,500 to 39,500. The same goes for people over the age of 50 (from 5,500 to 21,500).

By far the largest group of employment seekers was people with no previous work experience (128,400 in 1989 and 180,700 in 1997).

The situation was much better in all other groups of work experience:

Less than 1 year experience – from 6,300 (1989) to 7,900 (1997)

1-2 years – 3,500 to 5,000

2-3 years – 2,500 to 3,600

3-5 years – 3,400 to 5,700

5-10 years – 5,300 to 13,200

10-20 years – 3,200 to 18,200

20-30 years – 800 to 11,700

The number of unemployed people with more than 30 years experience went up – from 100 in 1989 to 3,100 in 1997.

The time structure of unemployment has also worsened.

In 1989 22,900 found employment within 6 months. In 1997 – there were only 6,100.

Within 6-9 months – from 8,300 to 4,100

Within 9-12 months – from 8,000 to 5,000

Between 1-3 years – from 51,300 to 71,600

Between 3-5 years – from 28,500 to 49,500 (!!!)

Between 5-8 years – from 20,700 to 49,900 (!!!)

More than 8 years – from 13,800 to 71,400 (!!!!!!!)

In other words, most of the employment seekers have to wait for years before they gain employment. About 30% of them wait for more than 8 years. This is nothing short of disastrous.

Unemployment is concentrated, therefore, among the relatively young and without work experience. Additionally, the skilled and highly skilled workers have lesser difficulties in finding a job. Only 46,000 of them were employment seekers in 1997 (compared to 26,000 in 1989). The semi-skilled and those with elementary school are the most vulnerable, with 132,800 employment seekers (versus 75,200 in 1989). Even those with secondary school training fared badly, with 74,200 employment seekers (versus 49,300 in 1989).

The Workforce Survey

Macedonia has executed a workforce survey for the first time in 1996. In this survey the following definitions were used:

Economically Active

The combined numbers of the employed and the unemployed

Employed

People aged 15 or more who worked for a wage (in cash or in kind) or had income during at least one hour during the reference week

Or

Were temporarily absent from work with a formal job assignment

Or

Were helping on the family property or enterprise without wages

Self Employed

An employer who operates his or her own enterprise or engages independently in a profession or trade or owns a farm and employs other people

Or

An employer who works for a private or public employer

Or

Own account worker – a person who operates his or her own enterprise or engages independently in a profession or trade but does not employ other persons

Or

An unpaid family worker – a person who works without pay in an enterprise, a trade, or on a farm owned by another member of his or her household.

Unemployed

Was without work during the reference week and ...

Was seeking work, i.e. has taken specific steps to find a job and ...

Was prepared to accept a job in the reference week or in the following week

Changes in the Labour Force

The activity rate as the ratio of the labour force in the total population above the age of 15 years

The employment rate as the ratio of the number of workers employed to the total population above the age of 15 years

The unemployment rate as the ratio between the numbers of the unemployed to the total labour force.

As of 4/97:

The total activity rate was 53.7% (66.5% for men and 41.2% for women). But this number hides major disparities in age groups. For instance: the activity rate of the age groups 35-39 was as high as 80.5% while for adolescents between the ages of 15-19 it was only 22.7% and for people between the ages 55-59 it was 36.5%.

The total employment rate was 34.4% (44.6% men and 24.4% women). Again, there were great disparities between age groups. The employment rate for ages 40-44 was 62.6% - while for ages 15-19 it was only 4.4% and for ages 20-24 it was a meager 18.2%.

The total unemployment rate was 36% (33% for men and 40.8% - women). More than 80.4% of the population aged 15-19 was unemployed, but only 20.2% of 40-44 and only 12% of 55-59.

The total population above the age of 15 at the time of the survey was 1,489,625 (men – 736,977 and women – 752,648).

The total labour force was 800,513 (men – 490,122, women – 310,392).

The total number of unemployed was 288,213 (men – 161,717, women – 126,496).

The total number of employed people was 512,301 (men – 328,404, women – 183, 896).

Outside the labour force there were 689,112 people (men – 246,856, women – 442,256).

To summarize in terms of percentages:

Ages 15-19 – 11% of the population – 4.6% of the labour force – 1.4% of the employed – 10.3% of the unemployed – 18.3% of those outside the work force.

Ages 20-24 – 10.3% - 12.4% - 5.5% - 24.8% - 7.9%

Ages 25-29 – 9.7% - 13.8% - 10% - 20.7% - 5%

Ages 30-34 – 9.5% - 13.8% - 13.4% - 14.3% - 4.5%

Ages 35-39 – 9.8% - 14.7% - 16.8% - 11% - 4.1%

Ages 40-44 – 9.7% - 14.1% - 17.6% - 7.9% - 4.5%

Ages 45-49 – 9% - 12% - 15.4% - 6% - 5.5%

Ages 50-54 – 6.9% - 7.3% - 9.8% - 2.8% - 6.4%

Ages 55-59 – 6.2% - 4.2% - 5.8% - 1.4% - 8.5%

Ages 60-64 – 6.7% - 1.8% - 2.6% - 0.4% - 12.4%

Ages 65-69 – 5.1% - 0.5% - 0.8% - 0% - 10.4%

Ages 70-80 – 0.4% - 0.3% - 0.3% - 0.2% - 0.6%

In the population above the age of 15 years as a whole, there were c. 104,000 without education, 199,000 with incomplete education, 474,000 with primary education, 151,000 with 3 years or less of secondary education, about 369,000 with 4 years of secondary education and c. 55,000 with a higher education. There were 81,100 with university degrees, 2,400 masters, 1,200 doctorates and 53,400 “other”.

Yet, the numbers in the labour force were very different and reflected the absolute disadvantage of the uneducated, unskilled, semi skilled and even those with only secondary education.

Those without education were 20,000 in the labour force, 12,000 among the employed, 8,000 among the unemployed (the employed and unemployed make up the labour force) - and a staggering 84,000 outside the workforce altogether.

The respective figures for those with incomplete education:
62,300, 44,200, 18,100, 136,300

For those with primary education (notice the marked improvement in employability!!!):
220,800, 118,000, 103,100, 253,100

And for those with 3 years of secondary education:

106,100, 64,800, 41,200, 45,100

Those with only one additional year of secondary education already look much better:

263,000, 176,000, 87,000, 106,300

And those with a higher education maintain European rates of unemployment:

41,000, 32,700, 8,300, 13,400

Those with university degrees:

67,200, 54,100, 13,100, 13,900

Masters:

1,630, 1,560, 70

Doctorates:

1,156, 1,086, 70, 71

76.3% of all men were employed (82.6% of women), 4.3% were employers (1.7%), 4.9% were self-employed (2.5%), 3.4% worked in family owned businesses (7.5%), 10.8% of all men worked in agriculture (and 5.6% of women).

Men made up 62.3% of the employed (women – 37.7%), 82.2% of all employers (17.8%), 78% of the self employed (22%), 45% of those employed in family businesses (55%), 77.5% of those employed in agriculture (22.5%).

The Situation in 8/99

Economic underdevelopment, agrarian over-employment, external shocks and an unrestructured economy led to an increase in both structural and cyclical employment.

The supply side is still composed mainly of new entrants, women and unskilled or semi-skilled labour as well as educated workers.

The demand structure is incompatible with the supply. It is made of replacement jobs, new jobs (mainly in labour intensive industries), jobs generated by foreign entities.

The number of the unemployed broke yet another record in 1999 and reached 344,472 people. Of these, almost half – 154,000 – were unskilled. But the unemployed included 5 doctors, 34 holders of master's degrees and 11,400 with higher education. About 33,000 of these numbers were made “technologically redundant” – the euphemism for being laid off due to restructuring of enterprises or their closure. By comparison, the number of employed people was only 316,000. In the first 8 months of 1999 alone there were 6,000 new unemployed per month versus a monthly average of 3,700 in 1998. This increase is attributed to the inclusion of people who did not bother to register with the Employment Bureau in the past.

The fiscal burden increased dramatically as contributions deteriorated to 25% of the Employment Bureau's financing while the state budget contributed the remaining 75%, or 3 billion MKD (equal to 100 million DM or c. 1.7% of GDP). The Employment Bureau also pays health insurance for about 200,000 unemployed workers.

The Labour Unions

The Association of Trade Unions in Macedonia (ATUM or CCM in the Macedonian acronym) is a voluntary organization, which encompasses 75% of all the employed workers in Macedonia as its members.

It is organized in the level of firms and institutions and has in excess of 2600 chapters. Additionally, it has about 150 chapters in the municipalities and in the various industrial sectors (all 15 of them).

The typical Macedonian trade union is not supported by the government and is entirely financed by its membership fees (self sufficient).

The first collective agreement was signed in 1990 at which time the idea of Economic Social Council was floated as well as the idea of a tripartite (government+employees+employers) dispute settlement mechanism.

The Labour Relations act was passed in 1994 and instituted national collective agreement for the economic sector between CCM and the Board of Employers of the Economic Chamber of Commerce of Macedonia. Another general collective agreement covered all public services, public companies, state organs, local authorities and legal persons performing non-

economic activities. This latter general collective agreement was signed between CCM and the Government of the Republic of Macedonia. Yet a third set of more than 20 collective agreements between CCM and various organs of the Chamber of Commerce and ministries covered other sectors.

The Future of Unemployment in Macedonia

Public enterprise restructuring, privatization and reform are likely to increase unemployment benefits by 200-300 million MKD annually (assuming only 2,000-3,000 workers are fired, a very conservative assumption as there are 18,000 workers in the 12 major loss making state firms, whose closure was demanded by the IMF).

Unemployment is very dependent on productivity and GDP growth. The World Bank predicts that with a GDP growth of 0%, the total expenditures on unemployment benefits could equal 2.3% of GDP. Even if GDP were to grow by 4% annually, their projections show unemployment benefits equaling 1.6% of GDP.

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V. Appendix – The Keynesian view of Unemployment, Stabilization Theory and Full Employment Budgeting

(From The Encyclopedia Britannica 1999 Edition)

A model of a Keynesian depression.

Involuntary unemployment.

Another possible cause of a general depression was suggested by Keynes. It may be approached in a highly simplified way by lumping all occupations together into one labour market and all goods and services together into a single commodity market. The aggregative system would thus include simply three goods: labour, commodities, and money. The [Table](#) provides a rough outline (a full treatment would be both technical and lengthy) of the development of a "Keynesian" depression. One may begin by assuming (line 1) that the system is in full [employment](#) equilibrium--that is, prices and wages are at their equilibrium levels and there is no excess demand. Next the model may be put on the path to disaster by postulating either (1) some disturbance causing a shift of demand away from commodities and into money or (2) a reduction in the money supply. Either event will result in the situation described in the [Table](#) as State 2, but the one assumed is a reduction in the money supply by, say, 10 percent. The result is shown in the right-hand column of the [Table](#), where the quantity of commodities supplied minus the quantity demanded multiplied by the price level (p) is equal in value to the excess demand for money.

If money wages and money prices could immediately be reduced in the same proportion (10 percent), output and employment could be maintained, and profits and wages would be unchanged in "real" terms. If money wages are initially inflexible, however, business firms cannot be induced to lower prices by 10 percent and maintain output. In this example they maintain prices in the neighbourhood of the initial price level--prices, then, are also "inflexible"--and deal with the excess supply by cutting back output and laying off workers. Reducing supply eliminates the excess supply of commodities by throwing the burden of excess supply back on the labour market. Thus, output and employment (which are "quantities") give way before prices do. This brings us to State 3 where, as in the [Table](#), the excess supply of labour times the money wage rate (w) equals the excess demand for money in value.

If, with the system in this state, money wages do not give way and the money supply is not increased, the economy will remain at this level of **unemployment** indefinitely. One should recall that the only explanation for persistent **unemployment** that the pre-Keynesian economics had to offer was that money wages were "too high" relative to the money stock and tended to remain rigid at that level.

Money wages might, nevertheless, give way so that, gradually, both wages and prices go down by 10 percent--that is to say, a reduction of the size that would have solved the entire problem had it occurred immediately (*before unemployment* could develop). This is shown in the last line of the [Table](#), which represents (albeit crudely) what Keynes described as a state of "involuntary **unemployment**" and explained in terms of a failure of "effective demand."

In State 4, it is assumed, the excess demand for money is zero. Hence there is, at least temporarily, no tendency for money income either to fall further or to rise. The prevailing level of money income is too low to provide full employment. The excess supply of labour and the corresponding excess demand for commodities (of the same market value) show State 4 to be a disequilibrium state. The question is why the state tends to persist. Why is there no tendency for income and output to increase and to absorb the **unemployment**? Specifically, why does not the excess demand for commodities induce this expansion of output and absorption of **unemployment**?

Basically, the answer is that the unemployed do not have the cash (or the credit) to make the excess demand for commodities *effective*. The traditional economic theory would postulate that, when actual output is kept at a level below that of demand, competition between unsuccessful potential buyers would tend to raise prices, thereby stimulating an expansion. But this does not occur. The unemployed lack the means to engage in such bidding for the limited volume of output. The excess demand for commodities is not effective. It fails to produce the market signals that would induce adjustments of activities in the right direction. Business firms, on their side of the market, remain unwilling to hire from the pool of unemployed--even at low wages--because there is nothing to indicate that the resulting increment of output can actually be sold at remunerative prices.

Keynes called this "involuntary **unemployment**." It was not a happy choice of phrase since the term is neither self-explanatory nor very descriptive. Some earlier analysts of the **unemployment** problem had, however, tended to stress the kind of deadlock that might develop if workers held out for wages exceeding the market value of the product attributable to labour or if business firms insisted on trying to "exploit" labour by refusing to pay a wage corresponding to the value of labour's product. With the term "involuntary **unemployment**," Keynes wanted to emphasize that a thoroughly intractable **unemployment** situation could develop for which neither party was to blame in this sense. His theory envisaged a situation in which both parties were willing to cooperate, yet failed to get together. An effective demand failure might be described as "a failure to communicate." (see also *Index*: [labour economics](#))

The failure of the market system to communicate the necessary information arises because, in modern economies, money is the only means of payment. In offering their labour services, the unemployed will not demand payment in the form of the products of the individual firms. If they did, the excess demand for products would be effectively communicated to producers. The worker must have cash in order to exercise effective demand for goods. But to obtain the cash he must first succeed in selling his services.

Effects of business [contraction](#).

When business begins to contract, the first manifestation is a decrease in investment that causes **unemployment** in the capital goods industries; the unemployed are deprived of the cash wage receipts required to make their consumption demands effective.

Unemployment then spreads to consumer goods industries. In [expansion](#), the opposite occurs: an increase in investment (or in government spending) leads to rehiring of workers out of the pool of unemployed. Re-employed workers will have the cash with which to exert effective demand. Hence business will pick up also in the consumer goods industries. Thus the theory suggests the use of [fiscal policy](#) (an increase in government spending or a decrease in taxes) to bring the economy out of an **unemployment** state that is due to a failure of effective demand. (see also *Index*: [business cycle](#))

Another observation may be made on Keynes's doctrine of effective demand. The fact that the persistence of **unemployment** will put pressure on wages also turns out to be a problem. The assumption in the foregoing discussion was that money wages were at the equilibrium level. **Unemployment** will tend to drive them down. Prices will tend to follow wages down, since declining money earnings for the employed will mean a declining volume of expenditures. In short, both wages and prices will tend to move away from, rather than toward, their "correct" equilibrium values. Once the economy has fallen into such a situation, Keynes pointed out, wage rigidity may actually be a blessing--a paradoxical conclusion from the standpoint of traditional economics. (see also *Index*: [production](#))

Stabilization theory.

The new stabilization policy needed a theoretical rationale if it was ever to win general acceptance from the leaders of public opinion. The main credit for providing this belongs to Keynes. In his [General Theory of Employment, Interest and Money](#) (1935-36) he endeavoured to show that a capitalist economy with its decentralized market system does not automatically generate [full employment](#) and stable prices and that governments should pursue deliberate stabilization policies. There has been much controversy among economists over the substance and meaning of Keynes's theoretical contribution. Essentially, he argued that high levels of **unemployment** might persist indefinitely unless governments took monetary and fiscal action. At that time he believed that fiscal action was likely to be more effective than monetary measures. In the deep depression of the 1930s, interest rates had ceased to exert much influence on the ways in which owners of wealth disposed of their funds; they might choose to hold larger cash balances instead of spending more money as the traditional theory had suggested. Nor were investors inclined to take advantage of low interest rates if they could not find profitable uses for borrowed funds, particularly if their firms were already suffering from excess capacity. Keynes's pessimistic view of monetary policy had a strong influence on economists and governments during and immediately after World War II, with the result that monetary policy was not tried very much during the 1940s. It was often forgotten during the policy discussions of the time that Keynes's views on the efficacy of monetary policy were related to the particular situation of the 1930s.

Another influential idea embodied in Keynes's writing was that of economic stagnation. He suggested that in the advanced industrial countries people tended to save more as their incomes grew larger and that private consumption tended to be a smaller and smaller part

of the national income. This implied that investment would have to take a continually larger share of the national income in order to maintain full employment. Since he doubted that investment would rise sufficiently to do this, Keynes was rather pessimistic about the possibility of achieving full employment in the long run. He thus suggested that there might be some permanent tendency to high levels of **unemployment**. This also had considerable influence on economic policy during the early postwar period; it was some time before those in decision-making positions realized that inflation, rather than stagnation and **unemployment**, was to be the main problem confronting them.

The desirability of pursuing policies to maintain high levels of employment was generally accepted in most industrial countries after the war. In 1944 the British government stated in its [White Paper](#) on Employment Policy that "the government accept as one of their primary aims and responsibilities the maintenance of a high and stable level of employment after the war." One of the most influential British economists at this time was Sir [William Beveridge](#), whose book *Full Employment in a Free Society* had a strong impact on general thinking. Similar ideas were expressed in the United States in the [Employment Act](#) of 1946, which stated: "The Congress hereby declares that it is the continuing policy and responsibility of the Federal Government to . . . promote maximum employment, production and purchasing power." The Employment Act was less specific as to policy than the British government's White Paper, but it established a council of economic advisers to assist the president and called upon him to present to every regular session of Congress a report on the state of the economy. The president was also required to present a program showing "ways and means of promoting a high level of employment and production." Similar programs were adopted in other countries. In [Sweden](#) in 1944 the Social Democrats published a document somewhat similar to the British White Paper, and other such declarations were made in Canada and Australia.

Full Employment Budget

Although the idea of budget balance in the administrative budget has been the dominant consideration in the budgetary policy of most countries, it has gradually been realized that such a concept may be inappropriate when external shocks such as exchange rate movements or a world recession occur. Because varying levels of [unemployment](#) are a major reason why expenditures may change without comparable change in the public sector output, the concept of a full-employment budget has emerged. This type of budgeting is based on receipts and expenditures that would prevail under conditions of full employment. The approach views the actual expenditures and receipts for the coming year as of secondary importance; it assigns primary importance to the influence of the budget on the national economy. In time of recession a budget deficit may thus be presented as a necessary step toward achieving a balanced budget at full employment. Ideally, the budget should include estimates of expenditures and revenues at full employment, and also estimates of the same items at the anticipated level of employment. These ideas have been extensively used in the United States.

An analogous procedure could be used with respect to inflation, but this idea is still far from acceptance, because governments are no less reluctant to anticipate inflation than they are to budget for **unemployment**.

The U.S. full-employment budget was developed during World War II and has been regularly published in the president's annual Economic Report since 1962. Other countries have adopted similar measures as an aid to policy-making; for example, The Netherlands' "structural budget margin," developed in the early 1960s, and West Germany's "cyclically neutral budget," calculated by its German Council of Experts beginning in the late 1960s.

III. Appendix – Unemployment throughout the World (excerpts from an academic article by R.di Tella and R. MacCullouch, 4/1999)

The Consequences of Labour Market Flexibility: Panel Evidence Based on Survey Data¹

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Abstract

We introduce a new data set on hiring and firing restrictions for 21 OECD countries for the period 1984-90. The data are based on surveys of business people in the countries covered, so the indices we use are subjective in nature. Controlling for country and time fixed effects, and using dynamic panel data techniques, we find evidence that increasing the flexibility of the labor market increases both the employment rate and the rate of participation in the labor force. A conservative estimate suggests that if France

¹ Address for correspondence: Rafael Di Tella, Harvard Business School, Soldier Field Road, Boston, Ma 02163, USA; e-mail: rditella@hbs.edu. Part of this research was carried out while the first author was a member of the Fundacion Mediterranea. We give thanks to Andrew Oswald and to Alberto Ades, Danny Blanchflower, Steve Bond, Lawrence Katz, Sebastian Galiani, Guillermo Mondino, Pascal Marianna, Edmund Phelps, Julio Rotemberg, Jurgen von Hagen, and to seminar participants at Deutsche Bundesbank, Dartmouth, Harvard, Oxford and Bonn for helpful discussions and suggestions.

were to make its labor markets as flexible as those in the US, its employment rate would increase 1.6 percentage points, or 14% of the employment gap between the two countries. The estimated effects are larger in the female than in the male labor market, although interestingly both groups seem to have similar long run coefficients. There is also some evidence that more flexibility leads to lower unemployment rates and to lower rates of long-term unemployment. The analysis of inflows and vacancies present some inconsistencies, although there is some evidence that the correlation between inflows and the business cycle is stronger in more flexible labor markets (again this is stronger for females). We also find some evidence consistent with the hypothesis that inflexible labor markets produce "jobless recoveries" and introduce more unemployment persistence.

JEL Classification: J65

Keywords: Job security provisions, subjective data, employment, and unemployment.

I. Introduction

One of the biggest challenges in economics today is to explain what causes European unemployment. Commentators on the European situation often blame poorly designed labor market institutions, a view that sometimes goes by the ugly name of "Eurosclerosis". Economists advising governments on these issues share more or less the same diagnostic: regulations such as hiring and firing restrictions faced by firms, as well as the generous welfare state that protects the unemployed, are behind the differential labor market performances of Europe and America. A number of countries have taken this view seriously. Great Britain and France are just two examples of countries that followed the economists' advice and reduced hiring and firing restrictions in the mid 1980's to combat high unemployment. This view of the labor market has also inspired large reform programs in the less developed world, where unemployment has recently increased. In fact, deregulation of the labor market is part of what the IMF and the World Bank often call "second generation reforms".²

Since unemployment brings real misery to people's lives, and job security provisions often involve delicate redistribution issues between richer firm owners and poorer workers, one would think that economists giving such advice know what they are doing. More precisely, one would think that there are hundreds of papers studying whether more flexibility in fact does reduce a country's unemployment rate in practice. Sadly, this is not the case. To our knowledge, there is one panel study on the effects of labor market flexibility across countries (Lazear (1990)).

² Labor flexibility is one of the main features of the IMF's recent agreement with Argentina, where unemployment reached an alarming 18.6% after the first 5 years of pro-market reforms.

And only a couple of cross-section studies, like the early one of Bertola (1990) based on evidence for 10 countries or that in the OECD Jobs Study (1994) based on 21 observations.³ Addison and Grosso (1996) revise Lazear's data and obtain different estimates with respect to unemployment (they find no evidence favoring the hypothesis that severance pay increase unemployment).⁴ Gregg and Manning (1997) review some of the available evidence on the effects of labor market flexibility and argue that it is *"much less persuasive than is commonly believed"*, and that the profession's *"faith in the merits of labor market de-regulation is misplaced"* (p.395). There is, perhaps, no experience more sobering to an economist than to review the state-of-the-art evidence on the effects of firing costs and to reflect on the social costs of unemployment.

The contribution of this paper is empirical. We introduce a new data set on hiring and firing restrictions for 21 OECD countries for the 7-year period covering 1984-90. The data are based on surveys of business people in the countries covered, so the indices we use are subjective in nature. We also use the new summary measure of the parameters of the unemployment insurance system compiled by the OECD in 1994, which constitutes a significant improvement on previous benefit data available in the profession. We then present an empirical analysis of the effect of flexibility on a number of labor market variables that follows and extends the contributions of Lazear (1990). Controlling for country and time fixed effects, and using dynamic panel data techniques developed by Arellano and Bond (1991), we find evidence that relaxing job security provisions increases the employment rate and the participation rate. The estimated effects seem large. The fixed effects estimate tells us that, if France were to reform its labor markets and make them as flexible as the American, its employment rate would increase by 1.6 percentage points.⁵ This is equivalent to 14% of the employment rate gap between the two countries. In order to express this effect in terms of GDP per capita, we note that it implies an increase in total employment of 2.8%. In the short run, the estimated effects are stronger for females than for males, although interestingly both groups have roughly similar long run coefficients. There is also evidence that a more flexible labor market leads to lower unemployment rates and to a lower proportion of long term unemployed in the unemployment pool. There is weaker evidence that flexibility leads to longer hours worked in manufacturing. The

³ There are even just a few in-depth single country studies. The interested reader is referred to the work of Abraham and Houseman (1994) and Hunt (1994).

⁴ Although they strongly emphasize a number of differences with Lazear's study (e.g. they also obtain different estimates with respect to advance notice requirements), it is worth noting that they find similar results with respect to three out of four variables.

⁵ France is the median country in terms of flexibility, though it's below the mean. See Table A for a full description of the data.

effect of unemployment benefits on these variables is less clear cut. As a general point we think it is reassuring that, in spite of using such a different approach, our results are not out of line with those obtained by Lazear. We also document the basic correlation of flexibility with inflows and the rate of unfilled vacancies, and review the hypotheses that inflexible labor markets produce "jobless recoveries", introduce more unemployment persistence and reduce the country's vulnerability to external shocks.

The main empirical evidence on the effect of labor market flexibility that we have available today is presented in Lazear (1990). He uses data on severance pay and periods of notice required before employment termination for 22 developed countries for the period 1956 to 1984, and finds some evidence that they have a negative relationship with the employment rate and a positive one with the unemployment rate. For example, Lazear finds that the amount of money paid to the worker as severance enters negatively and significantly in univariate regressions on country means (18 observations) explaining the employment rate, the participation rate and the number of hours worked per week. The coefficient on severance pay in the unemployment regression is positive but insignificant, however. In univariate regressions explaining the unemployment rate and the number of hours worked that include country dummies (468 observations), the coefficient on severance pay keeps its sign and turns significant. It is insignificant, however, when explaining the employment rate or the rate of labor force participation (where it also changes sign).

Lazear points out a number of limitations in these data. Amongst them is the fact that information on one type of worker (blue collar with ten years of service) is used as a proxy for the entire system. Second and more significantly, information on two types of institutions (amount of severance pay and months of advance notice before dismissal) are used to proxy for a large number of employment regulations that affect the flexibility of the labor market.⁶ Clearly, flexibility of the labor market could be affected without showing up in these two series. Third, it does not allow for the fact that countries differ in the degree of enforcement of these laws, and that other, perhaps informal, aspects may be more important than the written laws. Lastly, Lazear points out that "*for the most part, rules change once or twice during the period per country, so much of the mileage is cross-sectional*

⁶ For example, Grubb and Wells (1993) describe five other types of regulations that are relevant besides the restrictions on an employer's freedom to dismiss workers. These include limits on the use (or the legal validity) of fixed-term contracts; limits on the use of temporary work agencies, restrictions on weekly hours of regular or overtime work; limits on shift, weekend and night work; and limits on employer's use of part time work. The OCED Jobs Study (1994) notes that an employer's freedom to dismiss workers can be restricted by a number of requirements other than a requirement of advance notice. These include a requirement of authorisation by third parties (e.g. government, or trade union), provisions for appeal against unfair dismissal and the enforcement of these rules.

rather than time-series” (Lazear (1990) p.708). Yet, it is the best data that economists have available to study a most important set of issues.

The flexibility data used in this paper come from the *World Competitiveness Report* (WCR). The WCR requests the opinion of a number of top and middle managers (on average 1,531 each year) on the flexibility enterprises have to adjust things like compensation and employment levels to economic realities in each of the countries covered. By its nature, these data avoid some of the objections raised to the data used by Lazear. For example, it uses information provided by business people who, presumably, are in a position to judge what aspects of flexibility laws actually affect business conditions. Furthermore, it passes simple validation tests. For example, it correlates nicely with the index of “*strictness of employment protection legislation*” constructed for the OECD Jobs Study (1994), arguably the most complete measure available, for the one year where both types of data are available (1989). There are, of course, limitations to the data we use. The time series dimension of the panel is considerably shorter than that of Lazear’s (7 years versus 29). Importantly, the question asked is more vague than what ideally an economist would like to use. Furthermore, a lower set of answers in one country may simply reflect the fact that people there use a different cardinal ranking than people in other countries. Though some of these objections can be tackled in the empirical section, the fact remains that subjective responses should be treated with caution. However, we believe the topic to be of such economic and social significance, and the data that so far has been available to the profession to be of such poor quality, that a willingness to experiment with survey data is justified.ⁱ

On the theoretical side, Lazear (1990) points out that if markets are complete, mandated severance payments should not have real effects. The argument is that the firm-worker pair can undo the firing costs imposed on them by a reverse transfer from the worker to the firm at the onset of the employment contract. Bertola (1990) finds that job security legislation does not bias labor demand toward lower average employment at given wages in a simple dynamic economy. The intuition is that a firm subject to a positive shock will hire less workers than otherwise, but that firms subject to a negative shock will be less prone to firing. Thus employment fluctuations are dampened, but average employment may be unchanged. The evidence he presents is based on Emerson (1988) and is consistent with this view. Bentolila and Bertola (1990) present a model where firing costs actually increase long run employment. On the other hand, Hopenhayn and Rogerson (1993) study a general equilibrium model with entry and exit of firms and calibrate it using data on firm level dynamics. They show that a tax on job destruction equal to one year’s wage reduces the employment rate by roughly 2.5%. There are very large welfare costs in their model: the cost of the same tax in terms of consumption is over 2%. A recent paper by Alvarez and Veracierto (1998) extends Hopenhayn and

Rogerson (1993) by introducing frictions in a world without perfect insurance markets. They find that severance payments increase welfare. The reduction in firm layoffs and the increase in the agents' search efforts (because employment is more desirable) reduce unemployment enough to compensate for lower consumption levels (productivity also falls).

A recent paper by Bertola and Rogerson (1997) shows that we can have similar rates of job creation and destruction across countries despite there being very different degrees of labor market flexibility, if other institutions lead to wage compression. Thus, lower flows due to job security provisions, the argument goes, could be compensated by higher employer-initiated job turnover originating in the generosity of the European welfare state. Thus, the paper points to the importance of controlling for the generosity of the welfare state when investigating the effects of flexibility on the workings of the labor markets. All regressions in our paper include the new summary measure of the unemployment benefit system compiled by the OECD Jobs Study (1994). It is calculated as the pre-tax average of the replacement ratios for two earnings level, three family situations and three durations of unemployment. Although not perfect, the data begin to address some of the criticisms raised by Atkinson and Micklewright (1991) to the data previously used in the literature.ⁱⁱ

In section II we present the data while section III presents the empirical results. Section IV concludes.

ⁱ Put another way, the data that we use have different problems to the data previously used in the literature. Thus, we view this paper as complementing Lazear's approach with "hard" data.

ⁱⁱ A number of studies have found evidence that unemployment benefit generosity increases unemployment at the micro level (e.g. Katz and Meyer (1990)). Cross-country panel studies, on the other hand, have failed to uncover significant effects of unemployment benefits on the unemployment rate, once country and year fixed effects have been included. One of the potential reasons is that the benefit data used are very poor. For example, Layard *et al* (1990) uses the 1985 duration of unemployment benefits as an indicator of generosity for the whole sample.